

VZCZCXRO7118
PP RUEHGI RUEHRN
DE RUEHNR #0656/01 0661240
ZNR UUUUU ZZH
P 061240Z MAR 08
FM AMEMBASSY NAIROBI
TO RUEHC/SECSTATE WASHDC PRIORITY 4965
INFO RUEHXR/RWANDA COLLECTIVE PRIORITY
RUEH DU/AMCONSUL DURBAN 0155

UNCLAS SECTION 01 OF 02 NAIROBI 000656

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DEPT FOR AF/E, AF/EPS, AND OES/ENV
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E.O. 12958: N/A

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SUBJECT: KENYA CHANGES ITS BUDGET PRIORITIES AND TIGHTENS ITS BELT

REF: (A) 07 NAIROBI 2641 (B) 07 NAIROBI 1981

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11. (SBU) Summary: The Government of Kenya (GOK) is appropriately making plans to shift its budget focus to reconstruction and recovery in the wake of the post-electoral political crisis and resulting civil unrest. Enormous resources will be required, with over \$14.3 million already set aside initially for this purpose. Even with the February 28 power sharing agreement inked, it will take more than six months to really begin reconstruction work on the ground. Also, redirecting the \$2.9 billion in long-term development funding in the current year's budget from infrastructure to recovery means that the cost of doing business in Kenya will remain high, perpetuating a persistent deterrent to foreign investment, and thus further complicating long-term recovery. End summary.

Vision 2030 is No Longer a Priority

12. (SBU) In his budget speech of June 2007, Finance Minister Amos Kimunya said the FY-2007-08 budget (July 1-June 30, see ref A) was to focus on infrastructure, health, and education, i.e. long-term investments which were expected to lay the foundation for achieving the Vision 2030 goal of middle income prosperity by 2030 (see ref B).

However, the damage done in the wake of Kenya's post-electoral political crisis has changed the GOK's priorities. The GOK annually submits a budget supplemental in March, and the first priority in the FY-2008 supplemental and FY 2008-09 development budget will be reconstruction and recovery, which will take the lion's share of the budget. Investments originally intended to lay the foundation for Vision 2030 will be a second priority, according to GOK's Planning Secretary Stephen Wainana in a February 21 meeting with Econ

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Treasury Warns Ministries to Cut Spending

13. (U) In a February 20 circular, Ministry of Finance Permanent Secretary Joseph Kinyua ordered agencies to review their medium term

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expenditure framework (MTEF) reports to "rationalize priorities and allocate the resource envelope accordingly." In another February 20 circular to all Government accounting officers entitled "Implementation of Austerity Expenditure Measures in 2007/2008 Budget," Treasury said the 2007-08 budget had assumed that stability,

structural reforms, and higher exports and domestic demand would generate 6.4% growth and sufficient tax revenue. However, revenue collection is now likely to decline, while total expenditure is expected to rise, creating a larger financing gap than the deficit originally planned under the budget. The circular stated Treasury has already received requests for Sh52 billion (\$800 million) in additional spending, and will limit the additional spending to free secondary education, the strategic grain reserve and famine relief, support to displaced people, establishment of an endowment fund for victims of violence, and enhanced security. To help pay for these new needs, the circular ordered all departments to cut their recurrent expenditures as follows:

Training - 25%
Foreign travel: 25%
Domestic travel: 20%
Purchase of office furniture and equipment: 40%
Expenses for boards, committee conferences, seminars, retreats and workshops - 24%

14. (U) In addition, the circular ordered agencies to freeze all recruitment and purchase of vehicles, even those already approved, except for security-related operations. Development projects which are not likely to start this fiscal year should be deferred to the next financial year.

Cost of Reconstruction Not Known

15. (U) Permanent Secretary of Housing Tirop Kosgey told a press briefing on February 21 that the full cost to the government of helping the internally displaced victims of post-election violence to resettle and rebuild is not yet known. Kosgey said that a team has been carrying out an inventory of the damaged property and will issue its report in a week's time. He claimed reconstruction would start by the end of March, subject to approval by all government agencies. Except where there is urgent need for government services, the PS said the reconstruction efforts would give priority to private homes over state-owned accommodations. The exercise will not entail a value-for-value reconstruction, but will stick to one standard for

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every house. According to Kosgey, the GOK will embrace cost-effective methods in the reconstruction, for which it has already set aside Ksh1 billion (about \$14.3 million).

Comment

16. (SBU) In the past, GOK ministries have often turned back as much as 70% of their development budgets each year because of implementation delays related to capacity and other constraints. In the current context, this is good news, because it means the GOK will be able to shift funds fairly quickly to recovery and reconstruction, where they are more urgently needed. Where the reconstruction will be carried out depends on whether or how soon displaced people are willing to return to their destroyed homes. Implementation is also critical. In the past, Kenyans, in government, companies, and as individuals, have taken advantage of disasters such as famines and floods to siphon off GOK and donor funds. Redirecting the current year's \$2.9 billion development budget away from improving infrastructure also means Kenya's high business costs will persist, a deterrent to investors that will hinder long-term recovery. End comment.

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